IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 116 of 1985

For Approval and Signature:

Hon'ble CHIEF JUSTICE MR DM DHARMADHIKARI
and
Hon'ble MR.JUSTICE A.R.DAVE

==========

1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : NO

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the Civil Judge? : NO

DAMODAR K. SHAH

Versus

COMMISSIONER OF INCOME-TAX

Appearance:

MR KH KAJI for Petitioner

MR Akil Qureshi with Mr M.R.Bhatt for Respondent No. 1

CORAM : CHIEF JUSTICE MR DM DHARMADHIKARI
and
MR.JUSTICE A.R.DAVE

Date of decision: /11/2000

CAV JUDGEMENT

(Per : CHIEF JUSTICE MR DM DHARMADHIKARI)

For the assessment years 1979-80 and 1980-81, at the instance of the assessee, the following three questions of law based on interpretation of section 64 (1) (iv) of the Income tax Act, 1961, have been referred and all the three questions deserve a common answer:

"(1) Whether on the facts and in the circumstances of the case, the tribunal was right in law in holding that there was any transfer directly or indirectly by the assessee to his wife within the meaning of section 64,Income tax Act, 1961 when the assessee took out a policy of insurance under section 6 of the Married Women's Property Act, 1874?

(2) If question No.1 is answered in the affirmative, whether on the facts and in the circumstances of the case, the tribunal was justified in law in holding that there was consideration for the said transfer within the meaning of section 64,Income tax Act, 1961 ?

(3) Whether on the facts and in the circumstances of the case, the interest earned by the wife of the assessee on the amount received on maturity of the insurance policy taken by the assessee under the Married Women's Property Act,1874 was includible in the income of the assessee under section 64 of the Income tax Act, 1961 ?"

All the three questions mould down to one common question as stated by the Tribunal, as to whether there was any transfer of asset by the assessee as the husband to his wife and whether it was without any consideration and interest income derived by the wife on the maturity value of the insurance policy can be taxed as income of the husband by recourse to section 64 (1) (iv) of the Act.

Provisions of section 64 (1)(iv) of the Act read:

"64 (1) In computing the total income of any individual, there shall be included all such income as arises directly or indirectly-

(i) x x x x

(ii) x x x x

(iii) x x x

(iv) subject to the provisions of clause (i) of section 27, to the spouse of such individual from assets transferred directly or indirectly to the spouse by such individual otherwise than for adequate consideration or in connection with an agreement to live apart;" (underlining by court).

Now, the facts leading to the Reference of the above questions be stated. The assessee had taken out a policy on his life for the benefit of his wife. It is purported to have been issued under the provisions of Married Women's Property Act, 1874, the provisions of which are not directly relevant for deciding the questions of income tax liability of the husband on the interest income from the maturity value of the policy. It may merely be mentioned that the aforesaid Act of 1874 was enacted with an object that insurance policy taken by the husband for the benefit of his wife should be treated as separate property for the wife and kept protected by exempting it from attachment for recovery of any dues against the husband .

Under the aforesaid insurance policy for which premium was paid by the husband, the wife received certain amounts and earned interest of Rs. 2,250/- thereon. The Income Tax Officer added the interest amount to the income of the husband under section 64 (1) (iv) of the Act.

The Commissioner of Income tax (appeals) allowed the appeal of the assessee and took the following view which stated in his own words is as under :

"The obligation to pay the premium is under the contract; it cannot,therefore, be said that the premia amounts are the assets transferred by the assessee for the immediate or deferred benefit of his wife. "

The Commissioner of Income tax (appeals) also referred to section 6 of the Married Women's Property Act and observed:

"The policy of insurance effected by husband in favour of his wife enures for her benefits. It is deemed to be a trust and the policy amount is never considered as property of the husband. The said amount cannot be held as property transferred by the husband to the wife directly or indirectly. The premia paid are also under the bilateral agreement or contract between the husband and the insurance company. The payments are by way of satisfaction of contractual liability. They cannot, therefore,be construed to be transfer of money by the husband to the wife with or without consideration. Accordingly, it cannot be said that either the policy amount becoming payable on the maturity of the policy or the amount of premia paid was an asset transferred directly or indirectly to the wife. The interest income is,therefore, not liable to be charged to tax in the hands of the appellant under section 64 of the Act."

The Tribunal, however, reversed the view of the CIT and agreeing with the opinion of the ITO held that interest earned on the maturity value of the policy was income from the asset transferred indirectly by the husband to the wife within the meaning of section 64 (1) (iv) of the Act. The Tribunal placed reliance on the decision of the Delhi High court in the case of A. C. Khanna vs. CIT (1968) 68 ITR 159, of the Bombay High Court in the case of D. M. Netarwala vs. CIT (1979) 120 ITR 848 and R.Dalmia (decd.) vs. CIT, (1982) 133 ITR 169.

Mr. K.H.Kaji appearing for the assessee in assailing the conclusion of the Tribunal in its order submits that premium amount for the policy was paid under contract of insurance. Under the contract of insurance, full agreed sum was payable in the event of premature death of the husband during the currency of the policy and maturity value of the amount of insurance was payable on payment of entire amount of premium . The premium amount paid for the insurance policy, according to his argument, is not an `asset' transferred directly or indirectly to the wife. The interest income earned on the amount received on the maturity value of the policy was not includible in the income of the husband under section 64 (1) (iv) of the Act. Very strong reliance has been placed on two decisions of the Supreme court in the case of CIT vs. Keshavlal Lallubhai Patel, (1965) 55 ITR 637. By relying

on the aforesaid decision, it is submitted that the word `transfer' used in section 16 (3) (a) has to be strictly construed to include within the word `transfer' only transfers in the strict sense.

On the facts found in the case of Keshavlal Lallubhai (supra) it was held by the Supreme court to be a case of non-transfer. There, the assessee had thrown all his self acquired property in the common hotchpotch of the property of Hindu Undivided Family consisting of his wife and sons. Some time later, an oral partition was effected and properties were transferred in accordance with the arrangement in the partition between the members of the family. The question was whether this amounted to `indirect transfer'; of the property allotted to the wife. The Supreme court held that partition of the joint family property was not a transfer in the strict sense. The above decision in Keshavlal Lallubhai (supra) is not helpful in the present case on facts here which are totally different. That was a case of partition of joint family property which included the property thrown by the assessee in the common hotchpotch. The Supreme court took the view that partition of the joint family property does not involve transfer. Partition is really a process in and by which a joint enjoyment is transformed into an enjoyment in severality.

On behalf of the assessee, second case relied of the Supreme court is CIT vs. Prembhai Parekh , (1970) 77 ITR 27. Relying on the said decision, the contention advanced on behalf of the assessee is that there is no direct or proximate connection between the transfer of asset and the income derived. The income in question does not arise directly as a result of transfer nor does in any manner connect with it. In the case of Prembhai Parekh (supra), the assessee was a partner in a firm having 7 Annas share therein. He retired from the partnership. Thereafter, he gifted certain amounts to each of his four sons. The firm was reconstituted . The question was - whether income arising to his minor sons by virtue of their admission to the benefit of the partnership firm could be included in the income of the assessee. It is on those facts that the Supreme court took the view that income earned by the minor sons as members of the partnership firm cannot be held to have proximity or direct connection with the gifts made by the assessee to his sons. The Supreme court found that there was no nexus between the transfer of asset and income in question. The proximity between transfer of asset and income is not on the basis of time or period.The aforesaid decision of the Supreme court in the case of

Prembhai Parekh (supra) came up for consideration in the later decision of the Supreme court in CIT vs. Smt.Pelleti Sridevamma, (1995) 216ITR 826 and Prembhai Parekh case (supra) was explained thus:

> "The proximity referred to is the proximity between the assets transferred and the income in question. The time lag, if any, is of no significance under section 64 (1) (iv) of the Act."

It was in this manner that this decision was understood and distinguished in the subsequent decision of the Supreme court in Smt Mohini Thapar vs. CIT (1972) 83 ITR 208. In the decision of Smt.Pelleti (supra), the facts on which the income was included in the income of the husband deserve to be noted for answering the questions posed before us. In the case of Smt.Pelleti (supra), the assessee as an individual was carrying on business in mica mining . She made cash gift of Rs. 90,000/- to her minor son.The amount was utilised for purchasing house property. The house property was utilised for assessee's business. After eight years, the house property was sold on which capital gain was derived as income. The question was whether this capital gain could be included in the income of the assessee. The Supreme court held:

> "What was gifted by the assessee to her minor son was cash of rupees ninety thousand but it could not be forgotten that that money was utilised for purchasing the said house property.It was only a case of substitution of one form of property by another form of property. When the said house property was sold, a capital gain of rupees fifty eight thousand was made. Capital gain is undoubtedly a type of income. The definition of `income' in section 2 (24) includes `capital gains'. It was,therefore, liable to be included in the income of the assessee."

Proximity between asset and income has to be considered irrespective of time lag between transfer of asset and actual income derived. The decisions of the Supreme court in Prembhai Parekh (supra) as explained in Smt

Pelleti (supra) were considered by the Division Bench of this court in CIT vs. Mehmoodmian Topiwala, (1995) 213 ITR 615..The decision in Prembhai Parekh (supra) is explained and later decision was taken note of. In the Division Bench case of this court in Topiwala (supra), the facts were that the assessee and his two brothers were joint owners of piece of land. The assessee gifted his one third share in the land to his brother's sons. The assessee's brother, on the same day, transferred one third share to the assessee's wife. The assessee's wife sold the land received by her. The amounts received by the wife of the assessee were invested by her with the assessee on which she had earned interest. ITO included the interest in the total income of the assessee and the Division Bench upheld such inclusion by observing:

> "Here, we are dealing with income which has a proximate connection with the transfer of the asset made by the assessee. On a plain reading of section 64 (1) (iv), it is evident that the income arising to the wife has to be included in the total income of her husband."

Learned counsel Mr. Akil Qureshi appearing for the revenue submits that the facts of this case clearly show that assets in the shape of amounts of premia were transferred by the husband in favour of his wife through the insurance policy and the interest amount derived from the maturity value of policy was clearly an income which arose indirectly from the asset transferred to the wife. Provisions of section 64 (1) (iv) are clearly satisfied in the present case. On behalf of the revenue, apart from the decisions of the Supreme court referred above, strong reliance has been placed on the decision of the Supreme court in CIT vs. Keshavji Morarji, (1967) 66 ITR 142. In the case of Keshavji Morarji (supra), the assessee had a son and three daughters. Keshavji Morarji transferred a sum of Rs. 5,00,000/- to his son.Later, by a deed, he settled Rs. 4,41,000/- in favour of his minor grand children and on the same day, his son settled a sum of Rs. 1,54,000/- upon his three sisters. ITO held that settlement indirectly transferred the asset belonging to his minor daughters. His son had transferred the asset belonging to the assessee to his own minor children. According to the assessing officer, the income attributable to his daughters is liable to be assessed in the hands of the assessee Keshavji Morarji. It is on

these facts that the Supreme court held against the assessee by treating the income of his minor daughters to be his income from the asset indirectly transferred. The Supreme court relied on its earlier decision in CIT vs. C. M.Kothari, (1963) 49 ITR 107. The observations and relevant provisions of the Act in the case of Kothari (supra) were quoted which read as under :

> "It is true that the section says that the assets must be those of the husband, but it does not mean that the same assets should reach the wife. It may be that the assets, in the course of being transferred, may be changed deliberately into assets of a like value of another person.
>
> A chain of transfer, if not comprehended by the word `indirectly', would easily defeat the object of the law which is to tax the income of the wife in the hands of the husband, if the income of the wife arises to her from assets transferred by the husband".

In the above factual and legal background, the questions posed before us have to be answered. For the purpose of application of section 64 (1) (iv) of the Act, the following conditions should be satisfied:

(1) There must be transfer of asset by the assessee to his wife;

(2) The transfer in favour of wife by the assessee must be otherwise than for adequate consideration, and

(3) The income in question should have arisen or accrued to the wife directly or indirectly from the asset transferred to her by her husband.

So far as condition No. (1) is concerned, it is, according to us, satisfied. The amount of premia paid by the husband for the benefit of wife to the insurance company under the insurance policy has to be held to be transfer of cash asset by the husband to the wife. We are not prepared to accept the submission made on behalf of the assessee that the amounts of premia were paid under the contract of insurance and to discharge contractual obligations under the insurance policy. What is to be noted in the opening part as also in clause (iv)

of section 64 is that there is use of expressions `directly or indirectly' at two places. If the income arises indirectly from the asset transferred by the assessee indirectly to his spouse, the income is includible in the income of the assessee. The provision has to be construed in a manner so as to fulfil the object of the Act which, as held by the Supreme court in Keshavji Morarji (supra) is to tax the income of wife in the hands of the husband, if the income of the wife arises to her from the asset transferred by the husband. Merely because the policy of insurance by its terms requires payment of premia by the husband during his life time, does not mean that premia were not cash amounts transferred to the benefit of the wife through the insurance policy. The provisions of the Married Women's Property Act, 1874 to which reference has been made by the CIT, are totally irrelevant. The said Act is intended only for the purpose of making the insurance amount as separate property of the wife and to make it exempt from attachment for recovery of dues against the husband. The amount of policy is the property of the wife under the said Act, but the income derived by way of interest on investment of maturity amount of the life insurance policy can be held to be income indirectly arising to the husband from the cash amounts paid as premia by him under the policy for the benefit of the wife. The maturity value of policy along with interest would be the exclusive property of the wife in accordance with the Act of 1874, but the interest amount is liable to be taxed as income of the husband in his hand.

So far as condition No. (2) is concerned, it is undoubtedly transfer of cash by the husband in favour of the wife otherwise than for any consideration. Condition No. (2) is also satisfied.

So far as condition No. (3) is concerned, what is required to be fulfilled is that the income should accrue indirectly or directly to the husband through the asset transferred. As discussed above, the amounts of cash premia paid under the insurance policy for the benefit of the wife resulted into payment of maturity value of the policy to the wife. The wife invested that amount and earned interest. This interest income, as observed above, arises as indirect income to the husband from the cash money transferred in the shape of premia towards the insurance policy for the benefit of the wife. Condition No. (3) is also fulfilled.

We are fortified in our conclusion by the decision of the Supreme court in the case of Keshavji Morarji (supra) and

the Division Bench decision of this court in the case of Topiwala (supra) which has considered all the decisions of the Supreme court on which reliance has been placed on behalf of the assessee. We are also fortified in our view by the decision of the Bombay High court in the case of Sevantilal Maneklal Sheth vs. CIT, (1965) 57 ITR 45. The facts of that case are nearer to the facts of the present case. There, the assessee made a gift to his wife of shares in a limited company. The wife sold the shares and made capital gain. The wholesale proceeds were invested and fetched annual interest. The question was- whether capital gain realised and the interest received annually were income arising from the shares transferred to the wife and can be included in the income of the husband. The Division Bench of the Bombay High Court came to the following conclusion against the assessee:

> "The transferred asset in the new form i.e. transformed into cash being only of the value of Rs. 69,730.- , the interest attributable to that amount would be the income from the transferred assets arising directly or indirectly from the transferred assets to the wife otherwise than for adequate consideration or in connection with an agreement to live apart within the meaning of section 16 (3) (a) (iii) and the rest of it would undoubtedly be the income of the wife but it was not the income from the transferred assets but it was the income from the income, which she had received during the previous year."
>
> In our opinion, therefore, out of the interest received by Bai Laxmibai for the subsequent years 1958-59 and 1959-60 only such interest as would be attributable to the value of the transferred assets viz. the amount of Rs. 69,730/- would be liable to be included in the total income of Maneklal and not the rest."

Applying the ratio of the decision of the Bombay High court to the facts of the present case, it is to be found that the maturity value of the policy was the amount of premia paid inclusive of other money like bonus or interest payable under the policy. This maturity value of the policy was invested by the wife to earn interest income. The interest income earned by the wife by deposit/investment of the maturity value of the insurance policy was income which arose indirectly from the cash

asset transferred by the husband in the shape of premia to the wife under the terms of the policy. In the present case,therefore, full amount of interest derived in respect of the amount of maturity value of the policy was liable to be included as income of the husband under section 64 (1) (iv) of the Act.

As a result of the detailed discussion aforesaid, three questions which have been considered as one common question are answered in favour of the revenue and against the assessee. Reference thus stands disposed of in favour of the revenue, but without any order as to costs.

(D. M. Dharmadhikari, C.J.)

(A. R. Dave,J.)

parekh